

Report
of the
Examination of
Security Health Plan of Wisconsin, Inc.
Marshfield, Wisconsin
As of December 31, 2002

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Jorge Gomez, Commissioner

Wisconsin.gov

August 7, 2003

125 South Webster Street • P.O. Box 7873
Madison, Wisconsin 53707-7873
Phone: (608) 266-3585 • Fax: (608) 266-9935
E-Mail: information@oci.state.wi.us
Web Address: oci.wi.gov

Honorable Jorge Gomez
Commissioner of Insurance
Madison, Wisconsin

Commissioner:

In accordance with your instructions, a compliance examination has been made of
the affairs and financial condition of:

SECURITY HEALTH PLAN OF WISCONSIN, INC.
Marshfield, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Security Health Plan of Wisconsin, Inc. (the HMO), was conducted in 1998 as of December 31, 1997. The current examination covered the intervening period ending December 31, 2002, and included a review of such 2003 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the HMO's operations, and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Provider Contracts
- Territory and Plan of Operations
- Affiliated Companies
- Growth of the HMO
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing

Emphasis was placed on the audit of those areas of the HMO's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the HMO to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the HMO's operations is contained in the examination work papers.

The HMO is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

II. HISTORY AND PLAN OF OPERATION

Security Health Plan of Wisconsin, Inc. (Plan or SHP), is a nonprofit network health maintenance organization (HMO) insurer. An HMO insurer is defined by s. 609.01 (2), Wis. Stat., as "a health care plan offered by an organization established under ch. 185, 611, 613, or 614, Wis. Stat., or issued a certificate of authority under ch. 618, Wis. Stat., that makes available to its enrolled participants, in consideration for predetermined fixed payments, comprehensive health care services performed by providers selected by the organization." Under the network model, the HMO provides care through contracts with clinics and otherwise independent physicians operating out of their separate offices. HMOs compete with traditional fee-for-service health care delivery.

SHP is sponsored by Marshfield Clinic (Clinic) and was incorporated on April 25, 1986, under the provisions of ch. 613, Wis. Stat., as a nonstock service insurance corporation, and commenced business the same day. SHP is a tax-exempt organization as described in s. 501(c) (4), Wis. Stat., of the Internal Revenue Code and is exempt from federal and state income taxes. The Clinic controls SHP through representation on the board, contracts, and common management.

SHP has 2,750 affiliated providers, including ancillary providers, of which there are 752 specialists, 636 primary care physicians, and 1,362 non-physician providers. Contracts with hospitals and affiliated providers include hold-harmless provisions for the protection of policyholders. Referrals outside of the network require prior approval of the SHP medical director.

Upon membership in some of its products, every member is encouraged to select a primary care physician. Participating primary care physicians may be from general practice, family practice, general internal medicine, obstetrics/gynecology, and pediatrics. These physicians agree to provide high-quality, cost-effective medical care to members 24 hours a day, 7 days a week.

SHP contracts with the Clinic for the provision of health care services provided to SHP participants within the Clinic system. The Clinic is paid a per-member-per-month capitation.

The Clinic is at risk for capitation shortfalls, if any. The contract became effective on January 1, 1996, and has a term of one year for each year thereafter. The contract automatically renews for a one-year term unless either party gives notice to the other party to terminate 60 days prior to the end of a contract year. In addition, either party, upon 90 days advance written notice at any time, may terminate the contract for cause. Physician services rendered by affiliated providers are based on discounted fee-for-service rates, which are subject to SHP fee maximums.

For Medicare services, the providers accept assignment for Medicare Part B services. SHP pays a discounted rate on charges for services in excess of the Medicare deductibles and for plan benefits not covered by Medicare.

In accordance with the contract's hold-harmless provision and Wisconsin law, affiliated providers may not seek compensation from participants for covered services, but must look exclusively to SHP for payment. An agreement to abide by this provision is mandatory for all affiliated providers and opting out of this requirement constitutes good cause for termination.

SHP contracts with Medco Health Solutions, Inc., to provide a pharmacy network, adjudication of pharmacy claims and implementation of the SHP Formulary. SHP pays the pharmacies for the covered prescriptions and supplies dispensed to participants.

SHP contracts with Allied Health of Wisconsin, S.C., to provide chiropractic services. SHP pays a per-member-per-month capitation to Allied Health of Wisconsin, S.C.

SHP contracts with 31 hospitals to provide inpatient services. Hospitals are reimbursed on a discounted fee-for-service basis. The following is a list of hospitals in which participating physicians have admitting privileges.

Hospitals with Affiliated Hospital Agreements

Black River Memorial Hospital	Black River Falls
Bloomer Community Memorial Hospital	Bloomer
Chippewa Valley Hospital	Durand
Cumberland Memorial Hospital	Cumberland
Eagle River Memorial Hospital	Eagle River
Flambeau Hospital Inc.	Park Falls
Good Samaritan Health Center	Merrill
Hayward Area Memorial Hospital	Hayward
Health South/Oakleaf Surgery Center	Eau Claire
Howard Young Medical Center	Woodruff
Indianhead Medical Center	Shell Lake
Lakeview Medical Center	Rice Lake
Langlade Memorial Hospital	Antigo
Memorial Health Center	Medford
Memorial Hospital	Neillsville
Memorial Medical Center	Ashland
North Central Health Care Facility	Wausau
Norwood Health Center	Marshfield
Oakleaf Surgical Hospital LLC	Eau Claire
Osseo Area Hospital	Osseo
Riverside Medical Center	Waupaca
Riverview Hospital	Wisconsin Rapids
Rusk County Memorial Hospital	Ladysmith
Sacred Heart Hospital	Eau Claire
Sacred Heart Hospital	Tomahawk
St. Josephs Hospital	Chippewa Falls
St. Josephs Hospital	Marshfield
St. Marys Hospital	Rhineland
St. Michaels Hospital	Stevens Point
Victory Medical Center	Stanley
Wausau Hospital Inc.	Wausau

Hospitals with Referral Arrangements and Pricing Agreements

Abbott Northwestern Hospital	Minneapolis
Children's Health Care	Minneapolis
Children's Hospital	Milwaukee
Children's Memorial Hospital	Chicago
Fairview University Medical Center	Minneapolis
Froedtert Memorial Hospital	Milwaukee
Libertas Treatment Center	Green Bay
Luther Hospital	Eau Claire
Milwaukee Psychiatric Hospital	Milwaukee
Rogers Memorial Hospital	Oconomowoc
St. Luke's Medical Center	Milwaukee
University of Wisconsin Hospitals	Madison

Effective December 1, 1996, SHP contracted with the Department of Health and Family Services (DHFS) of the State of Wisconsin to participate in the Medicaid HMO program. SHP maintains the Medicaid program as a separate operating division. The program expanded in 2000 to include the BadgerCare population. SHP has contracted with the Clinic and affiliated providers on a fee-for-service rate comparable to the State of Wisconsin Medicaid fee-for-service rate. Hospitals are paid based on Diagnostic Related Groupings (DRGs). The SHP Medicaid program does not include chiropractic or dental services.

According to its business plan, SHP's service area is comprised of the following counties:

Adams	Dunn	Juneau	Pepin	Taylor
Ashland	Eau Claire	Langlade	Portage	Vilas
Barron	Forest	Lincoln	Price	Waupaca
Chippewa	Iron	Marathon	Rusk	Waushara
Clark	Jackson	Oneida	Sawyer	Wood

In addition, the following counties have limited areas where service is available:
Monroe, Shawano, Trempealeau, and Washburn.

SHP signed a contract with the Centers for Medicaid and Medicare Services (CMS) to provide a Medicare+Choice product (M+C) in its 28 county service area. In August 2002, SHP began marketing and enrolling Medicare beneficiaries into a Medicare+Choice product named Advocare. The product is marketed through employed representatives and features coordinated care, benefits in excess of Medicare, and a flat monthly premium, regardless of age. This product is monitored by CMS through monthly reports, routine site visits, and member feedback.

SHP formed a separate division called Security Administrative Services (SAS) to serve as a Third Party Administrator (TPA) for customers desiring to self-fund their health insurance risk. The product features administration, coupled with SHP's medical management expertise. Stop-loss coverage for TPA business is provided by insurers licensed to do business in the State of Wisconsin.

SHP offers comprehensive health care coverage through various plans to groups and individuals. Although covered benefits are somewhat consistent among groups, SHP is capable of designing benefit plans to meet the specific requests of employers. Individual policies come with a variety of benefit options, including a Medicare Select program. The following basic health care coverage is generally provided:

Physician services	Prosthetics/durable medical equipment
Hospital services	Mental health and alcohol chemical dependency
X-ray and laboratory services	Skilled nursing home
Dental services	Diabetic services
Maternity services	Home health care
Emergency services	Prescription drug copayment/catastrophic
Kidney disease treatment	Chiropractic care
Refraction	Ambulatory surgery
Hospice	Hearing exam
Certain transplants	

SHP offers a variety of mental health benefit options. Most frequently selected is the greater of 15 days or \$6,300 of inpatient mental health benefit. Outpatient mental health and AODA is limited to the greater of 25 visits or \$1,800 and transitional benefits are limited to the greater of 15 visits or \$2,700.00. Emergency services are covered at 100% after deductibles. Skilled nursing facility care is limited to 30 days under currently marketed products.

Plan coverage is contingent on non-emergency services being provided by affiliated physicians and hospitals or on the authorization of the SHP medical director. SHP also has a variety of copayment plans. The high-option plan provides first-dollar coverage with no deductibles or copayment. There are several lower-option plans with varying levels of deductibles ranging from \$0 to \$5,000.00. Participants may choose physicians and health care providers from a listing of affiliated physicians.

SHP currently markets to employer groups and individuals. Business is solicited through in-house sales consultants and independent sales agents. For some group policies, independent agents are paid commission on a sliding scale based on annual premium. Commission schedules for group plans range from 8.27% of the first \$15,000 of premium to .09% of premium in excess of \$2,000,000.00. Other commission schedules are not retrogressive, but range from a flat 2.5% to 4% of annual premium or a negotiated dollar amount per contract that is built into the premium. The commission for Medicare-select and direct-pay products is 5% of

annual premium. The Dairy Milk Check Deduction Program is 8% of annual premium. The second and subsequent year commission is subject to continuing new business requirements of SHP. The in-house sales consultants are paid base salaries plus incentives.

Premium is actuarially determined to obtain sufficient revenue to cover anticipated net incurred claims for the contract period plus allocated administrative expenses and a contribution of 3% of premium to contingency reserves.

For individual businesses there are currently five active pools, four non-Medicare and one Medicare select. Each of these pools has different age and family size factors, but they follow the same general underlying rules. There are no rate distinctions by location, gender or occupational status. Smoothing of experience within pools is done to assure that rates will be the same or higher for older ages, poorer health risks or better benefits in each pool.

For group business, distinctions are made for the age, gender and average family size makeup of a group. Further adjustment is made for the group's location, benefits and, within the limitations of Small Group Law, category of industry. A rate credit factor is applied to groups where medical underwriting is permitted. For renewal group business with more than 50 employees and for prospective group business where the information is available, the rate determination incorporates up to 12 months of the group's actual claim experience on a credibility-weighted basis as a modifier to the demographics and group characteristics. At approximately 400 average contracts, a group will reach full credibility so that its rates will be determined entirely on its own claim experience and not on the basis of pool rates.

The present medical conditions of all the group's members are considered for all renewal group business with up to 50 employees and at the request of marketing for renewal business of any size. The "anticipated experience" of premium rates is tested to determine if SHP is in compliance with small group law on premium rate levels and rate increase limitations.

SHP has developed procedures to be followed in the event of subscriber grievances. The company's internal grievance procedure provides that it will acknowledge the grievance in writing within five calendar days. The grievance will be reviewed and resolved by SHP administration within 30 days. If SHP is unable to resolve the grievance within 30 days, the time

period will be extended an additional 30 days upon written notification to the member. The grievant has the right to appear before the grievance committee. SHP also has, as required by Wisconsin law, procedures for resolving urgent care situation grievances within no more than 72 hours. In addition, the right to review by an independent review organization is offered after decisions involving adverse determinations and experimental treatment determinations.

III. MANAGEMENT AND CONTROL

Board of Directors

The bylaws call for at least six but not more than 15 directors consisting of Marshfield Clinic executive committee members. The board of directors consists of nine members. Board members serve two-year terms until re-elected or removed. Officers are appointed by the board of directors. The board members currently receive no compensation for serving on the board.

Currently, the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Timothy R. Boyle, M.D. Marshfield, Wisconsin	Physician – Otolaryngology	2004
Robert A. Carlson, M.D. Marshfield, Wisconsin	Physician – Pathology	2005
Daniel G. Cavanaugh, M.D. Chippewa Falls, Wisconsin	Physician – General and Thoracic Surgery	2004
Gary R. Degerman, M.D. Rice Lake, Wisconsin	Physician – Obstetrics and Gynecology	2005
Gary P. Mayeux, M.D. Marshfield, Wisconsin	Physician – Gastroenterology	2004
Douglas J. Reding, M.D. Auburndale, Wisconsin	Physician – Oncology	2004
Ivan B. Schaller, M.D. Wausau, Wisconsin	Physician – Internal Medicine	2005
David J. Simenstad, M.D. Woodruff, Wisconsin	Physician – Orthopedic Surgery	2005
Frederic P. Wesbrook, M.D. Marshfield, Wisconsin	Physician – Internal Medicine	2004

Officers of the Company

The officers elected by the board of directors and serving at the time of this examination are as follows:

Name	Office	2002 Salary
Frederic P. Wesbrook, M.D.	President	\$0*
Gary P. Mayeux, M.D.	Vice-President	0*
Robert A. Carlson, M.D.	Secretary	0*
David J. Simenstad, M.D.	Treasurer	0*

*The officers do not receive a salary.

Committees of the Board

The HMO's bylaws allow for the formation of certain committees by the board of directors. At the time of the examination the company had one active committee which is listed below:

Audit Committee

David Simenstad, M.D., Chair
Frederic Wesbrook, M.D.
Gary Mayeux, M.D.
Reed Hall
Barbara Kuhl
Gary Jankowski
Peter Ziegler

The HMO has no employees. Necessary staff is provided through an administrative services agreement with the Clinic. Under the agreement, effective October 7, 1986, the Clinic agrees to provide all reasonably necessary administrative and managerial services required for the efficient operation of the Plan. These services include, but are not limited to, plan administration, program planning and development, financial systems and services, claims administration, coordination of benefits, data processing, provider and subscriber services, peer review and utilization review services, account administration, marketing, and legal services.

The Plan pays the Clinic an agreed upon rate per member per month as compensation for services provided by the Clinic on behalf of the Plan. The prepayment is adjusted each month based on the previous month's actual cost. The term of the agreement is two years and automatically renews for two-year terms unless either party notifies the other of the

intent to terminate in writing six months prior to the end of the contract period. The HMO may terminate the agreement upon six months' written notice if default of standards or performance continues 30 days after notice of such default. The HMO may terminate the agreement upon six months' written notice showing good cause.

Financial Requirements

The financial requirements for an HMO under s. Ins 9.04, Wis. Adm. Code, are as follows:

	Amount Required
1. Minimum capital or permanent surplus	Either: \$750,000, if organized on or after July 1, 1989 or \$200,000, if organized prior to July 1, 1989
2. Compulsory surplus	The greater of \$750,000 or: If the percentage of covered liabilities to total liabilities is less than 90%, 6% of the premium earned in the previous 12 months; If the percentage of covered liabilities to total liabilities is at least 90%, 3% of the premium earned in the previous 12 months
3. Security surplus	The greater of: 140% of compulsory surplus reduced by 1% of compulsory surplus for each \$33 million of additional premiums earned in excess of \$10 million or 110% of compulsory surplus
4. Operating funds	Funds sufficient to finance any operating deficits in the business and to prevent impairment of the insurer's initial capital or permanent surplus or its compulsory surplus

Covered liabilities are those due to providers who are subject to statutory hold-harmless provisions.

In addition, there is a special deposit requirement equal to the lesser of the following:

1. An amount necessary to maintain a deposit equaling 1% of premium written in this state in the preceding calendar year;
2. One-third of 1% of premium written in this state in the preceding calendar year.

The HMO has satisfied this requirement for 2002 with a deposit of \$2,500,000 with the State Treasurer.

Insolvency Protection for Policyholders

Under s. Ins 9.04 (6), Wis. Adm. Code, HMOs are required to provide continuation of coverage for its enrollees. These requirements are the following:

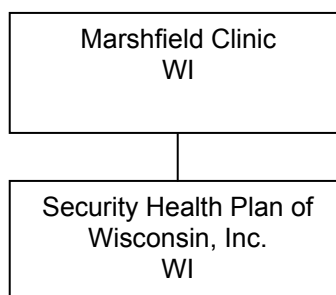
1. Enrollees hospitalized on the date of insolvency will be covered until discharged; and
2. Enrollees will be entitled to similar, alternate coverage which does not contain any medical underwriting or preexisting limitation requirements.

The HMO has met this requirement through its provider contracts, as discussed in the History and Plan of Operation section of this report.

IV. AFFILIATED COMPANIES

The HMO is a member of a holding company system. Its ultimate parent is Marshfield Clinic. The organizational chart below depicts the relationship among the affiliates in the group. A brief description of the significant affiliate of the HMO follows the organizational chart.

**Holding Company Chart
As of December 31, 2002**



Marshfield Clinic

Marshfield Clinic, founded in 1916, is a nonprofit group medical practice engaged in providing health care, health care education, medical research, and community service. With a medical staff of 707, and regional centers in 34 Wisconsin communities, the clinic has approximately 1,744,000 patient encounters annually. In addition to Wisconsin, patients from the entire Midwest visit the Clinic.

As of September 30, 2002, the company's audited financial statement reported assets of (in thousands) \$517,088 liabilities of \$308,769, and capital and surplus of \$208,319.00. Operations for 2002 produced net income/loss of \$26,586 on revenues of \$757,199.00.

V. REINSURANCE AND CORPORATE INSURANCE

The HMO has reinsurance coverage under the contract outlined below:

Reinsurer:	Allianz Life Insurance Company of North America
Type:	Specific Excess of Loss Reinsurance
Effective date:	August 1, 2002
Business Lines Covered:	Medicare + Choice
Retention:	Specific Deductible per Covered Person per Agreement Term: \$300,000
Coverage:	90% of Covered Expenses excess of Specific Deductible
Premium:	Medicare HMO: \$0.90 per member per month Medicare POS: \$0.90 per member per month
Termination:	July 31, 2003

The reinsurance policy has an endorsement stating: in the event of insolvency of SHP, all reinsurance will be payable directly to the liquidator, receiver, or statutory successor of SHP, on the basis of the liability of the reinsurer without diminution due to the insolvency of SHP. Marshfield Clinic, through its board resolution on October 6, 1992, has unconditionally guaranteed the financial and contractual obligations of SHP. The amended resolution regarding financial and contractual obligations of SHP states in part that (a) the Clinic will be responsible for the financial and contractual obligations of the plan and (b) the Clinic may enter into agreements with other facilities in the Plan's service area sharing of the potential financial and contractual obligations of the HMO. The HMO is deemed to be in compliance with s. Ins 3.50 (4) (e), Wis. Adm. Code, regarding insolvency protection of policyholders.

In addition, the HMO is provided with corporate insurance coverage under the contracts listed below:

Type of Coverage	Policy Limits
Directors' and officers' liability	\$10,000,000
Professional liability	10,000,000
Errors & Omissions	10,000,000
Umbrella Policy	10,000,000
General Liability	1,000,000

The above coverages were obtained through companies licensed in Wisconsin.

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the HMO as reported in the December 31, 2002, annual statement to the Commissioner of Insurance. Also included in this section are schedules that reflect the growth of the HMO for the period under examination. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Net Worth per Examination."

Security Health Plan of Wisconsin, Inc.
Assets
As of December 31, 2002

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$46,361,017	\$	\$46,361,017
Real Estate:			
Properties occupied by the company	48,782		48,782
Cash and short-term investments	13,325,882		13,325,882
Accident and health premiums due and unpaid	7,133,695		7,133,695
Health care receivables	1,497,616	400,000	1,097,616
Investment income due and accrued	693,955		693,955
Amounts due from parent, subsidiaries and affiliates	8,547,534		8,547,534
Amounts receivable relating to uninsured accident and health plans	8,294		8,294
Furniture and equipment	884,004	884,004	0
Electronic data processing equipment and software	1,293,475	985,108	308,367
Other nonadmitted assets	40,000	40,000	0
Aggregate write-ins for other than invested assets	<u>274,975</u>	<u>239,749</u>	<u>35,226</u>
Total assets	<u>\$80,109,229</u>	<u>\$2,548,861</u>	<u>\$77,560,368</u>

Security Health Plan of Wisconsin, Inc.
Liabilities and Net Worth
As of December 31, 2002

Claims unpaid		\$24,762,652
Unpaid claims adjustment expenses		598,000
Aggregate policy reserves		3,059,000
Aggregate claim reserves		150,000
Premiums received in advance		23,706,757
General expenses due or accrued		729,411
Borrowed money and interest thereon		1,781,144
Aggregate write-ins for other liabilities (including \$(1) current)		<u>584,035</u>
Total liabilities		55,370,999
Surplus notes	\$ 5,400,000	
Unassigned funds (surplus)	<u>16,789,369</u>	
Total capital and surplus		<u>22,189,369</u>
Total liabilities, capital and surplus		<u>\$77,560,368</u>

**Security Health Plan of Wisconsin, Inc.
Statement of Revenue and Expenses
For the Year 2002**

Net premium income		\$285,800,680
Medical and Hospital:		
Hospital/medical benefits	\$197,919,375	
Other professional services	13,844,316	
Outside referrals	3,466,556	
Emergency room and out-of-area	6,161,063	
Prescription drugs	<u>33,819,471</u>	
Subtotal	255,210,781	
Less		
Net reinsurance recoveries	<u>(4,137)</u>	
Total medical and hospital	255,214,918	
Claims adjustment expenses	4,595,556	
General administrative expenses	18,989,447	
Increase in reserves for accident and health contracts	<u>2,115,000</u>	
Total underwriting deductions		<u>280,914,921</u>
Net underwriting gain or (loss)		4,885,759
Net investment income earned		<u>2,462,327</u>
Net income (loss)		<u>\$ 7,348,086</u>

**Security Health Plan of Wisconsin, Inc.
Capital and Surplus Account
As of December 31, 2002**

Capital and surplus prior reporting year		\$15,563,393
Net income or (loss)	\$7,348,086	
Change in nonadmitted assets	<u>(722,110)</u>	
Net change in capital and surplus		<u>6,625,976</u>
Capital and surplus end of reporting year		<u>\$22,189,369</u>

Security Health Plan of Wisconsin, Inc.
Statement of Cash Flows
As of December 31, 2002

Cash from Operations		
Premiums and revenues collected net of reinsurance		\$286,736,734
Claims and claims adjustment expenses		256,111,541
General administrative expenses paid		<u>18,792,118</u>
Cash from underwriting		11,833,075
Net investment income		<u>2,673,518</u>
Net cash from operations		14,506,593
Cash from Investments		
Proceeds from investments sold, matured or repaid:		
Bonds	\$12,605,763	
Cost of investments acquired (long-term only):		
Bonds	<u>19,826,734</u>	
Net cash from investments		(7,220,971)
Cash from Financing and Miscellaneous Sources		
Cash applied:		
Net transfers to affiliates	1,236,764	
Borrowed funds repaid	54,231	
Other applications	<u>223,422</u>	
Total	1,514,417	
Net cash from financing and miscellaneous sources		<u>(1,514,417)</u>
Net change in cash and short-term investments		5,771,205
Cash and short-term investments:		
Beginning of year		<u>7,554,677</u>
End of year		<u>\$ 13,325,882</u>

Growth of Security Health Plan of Wisconsin, Inc.

Year	Assets	Liabilities	Capital and Surplus	Premium Earned	Medical Expenses Incurred	Net Income
2002	\$77,560,368	\$55,370,999	\$22,189,369	\$285,800,680	\$255,214,918	\$ 7,348,086
2001	62,966,993	47,403,600	15,563,393	256,213,364	237,289,331	2,302,923
2000	55,921,988	44,974,766	10,947,222	233,117,819	217,422,993	881,252
1999	45,112,140	36,306,170	8,805,970	170,618,710	162,308,475	(2,726,535)
1998	42,824,670	31,292,165	11,532,505	164,691,022	152,613,736	1,471,629
1997	39,632,865	29,571,989	10,060,876	141,007,891	128,287,733	3,612,692

Year	Profit Margin	Medical Expense Ratio	Administrative Expense Ratio	Change in Enrollment
2002	2.6%	89.3%	8.3%	(0.7)%
2001	0.9	92.6	7.4	(3.2)
2000	0.4	93.3	6.8	21.0
1999	(1.6)	95.1	8.2	(4.0)
1998	0.9	92.7	7.5	6.7
1997	2.6	91.0	7.5	25.0

Enrollment and Utilization

Year	Enrollment	Hospital Days/1,000	Average Length of Stay
2002	116,982	636.14	4.98
2001	117,786	639.15	4.96
2000	121,655	679.93	5.29
1999	100,515	610.71	4.65
1998	104,681	754.14	5.33
1997	98,146	381.02	3.84

Per Member Per Month Information

	2002	2001	Percentage Change
Premiums:			
Commercial	\$225.71	\$198.49	13.7%
Medicare	530.31	0.00	100.0
Medicaid	129.72	118.69	9.3
Expenses:			
Hospital/medical benefits	142.97	131.61	8.6
Other professional services	10.00	8.46	18.2
Outside referrals	2.50	2.96	(15.5)
Emergency room and out-of-area	4.45	5.49	(18.9)
Other medical and hospital	<u>24.43</u>	<u>20.83</u>	17.3
Total medical and hospital	\$184.35	\$169.35	8.9
Claims adjustment expenses	3.32	4.78	(30.5)
General administrative expenses	13.72	8.81	55.7
Increase in reserves for accident and health contracts	<u>1.53</u>	<u>0.08</u>	1812.5
Total underwriting deductions	<u>\$202.92</u>	<u>\$183.02</u>	10.9

Since the prior examination, the company's assets and surplus have increased 95.7% and 120.6% respectively. Enrollment increased 21% in 2000 and has decreased slightly in 2001 and 2002. Overall premiums have increased 102.7% while medical expenses incurred increased 98.9% from the prior examination. The company suffered a net loss in 1999 but has reported a net income each year since then with the largest net income being reported in 2002. The average length of stay has remained relatively the same for all years.

Reconciliation of Capital and Surplus per Examination

The examination did not result in any adjustments or reclassifications to surplus.

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were six specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the HMO are as follows:

1. Plan of Operations—It is recommended that the HMO comply with s. Ins 3.50(6), Wis. Adm. Code, as regards reporting any significant changes in the business plan

Action—Compliance

2. Financial Reporting—It is recommended that the HMO complete annual statement schedules according to National Association of Insurance Commissioners (NAIC) Annual Statement Instructions – Health Maintenance Organization.

Action—Compliance

3. Financial Reporting—It is recommended that the HMO report Medicare supplement premium and enrollment in the “individual” category for annual statement reporting purposes.

Action—Compliance

4. Investments—It is recommended that the HMO execute a custodial agreement in its own name and that such agreement contain required provisions in accordance with the NAIC Examiners Handbook.

Action—Compliance

5. Information Technology—It is recommended that the HMO store daily backups off site, or if daily backups are stored on-site, the backups should be stored in a secure, fireproof container.

Action—Compliance

6. Information Technology—It is recommended that the HMO formally develop a disaster recovery plan. The plan should identify procedures and persons responsible for the restoration of the HMO’s operations to a functional level. The recovery plan should be reviewed and tested at least annually.

Action—Compliance

Summary of Current Examination Results

Financial Reporting

The jurat page was signed by the President, Vice President, and Treasurer.

According to the annual statement instructions, the jurat page must be signed in accordance with the requirement of the state of domicile. Wisconsin domiciled insurers are required to have the notarized manual signatures of the President, Treasurer, and Secretary, except if the Treasurer does not have charge of the accounts of the insurer. The signature and title of the individual who has charge of the insurer's accounts should be entered. If appropriate corporate officers are incapacitated or otherwise not available due to personal emergency, Vice Presidents or Assistant Officers may sign the statement. In addition to the Secretary failing to sign the annual statement, the company did not list all members of the board on the jurat page. According to the bylaws, all officers and vice presidents are members of the board of directors. It is recommended that the company properly fill out the jurat page in accordance with the NAIC Annual Statement Instructions – Health pursuant to s. Ins 50.20, Wis. Adm. Code.

The Underwriting and Investment Exhibit, Part 2D shows the Aggregate Reserve for Accident and Health Contracts. Per the NAIC Annual Statement Instructions – Health, the premium deficiency reserve should be included in footnote (a); however, the company included this amount as a write-in. It is recommended that the company complete the Underwriting and Investment Exhibit – Part 2D, in accordance with the NAIC Annual Statement Instructions – Health pursuant to s. Ins 50.20, Wis. Adm. Code.

The examination revealed that the company reported on Schedule E – Part 2 one U.S. Treasury Note with a par value of \$580,000.00. The State Treasurer reported a par value of \$600,000.00. As a result a variance of \$20,000 was noted. The company noted that the amount exceeded the amount required by s. 609.98, Wis. Stat., by the \$20,000 amount. It is recommended that the company report the actual amount on deposit with the State Treasurer on Schedule E – Part 2, regardless of the amount required by statute as stated in the NAIC Annual Statement Instructions – Health.

Company Agreements

In reviewing the company's agreements with Marshfield Clinic, it was noted that the Administrative Agreement and the Maintenance Agreement do not include any indemnification or hold harmless provisions. The agreements with the Clinic should contain an indemnification clause to indemnify SHP for services provided. It is recommended that the company amend its agreements with Marshfield Clinic to include indemnification and/or hold harmless provisions.

Investments

The examination's review of the board of director minutes revealed that the board does not approve the company's investments. The accounting department of SHP and the treasury department of Marshfield Clinic have the authority to make the company's investment decisions. However, the board does not formally approve these investments. According to s. 611.67, Wis. Stat., a company may delegate management authority to a person other than an officer, director, or employee of the insurer if the person exercises the management authority according to the terms of a written contract between the insurer and the person, if the contract is filed and not disapproved by this office. The current arrangement is not a management agreement nor does it delegate investment review and approval authority. It is recommended the company establish procedures to have investment transactions formally approved by the board of directors.

Record Retention

The examination's review of a selected sample of group policy files noted that, in one instance, the group insurance policy was not located in the file and in three instances the group application was not located in the file. According to s. Ins 6.80, Wis. Adm. Code, contracts, benefits, applications, rates and rate changes, and letters discussing these changes be maintained and be readily available at the request of the commissioner. It is recommended that the company retain the appropriate records according to s. Ins 6.80, Wis. Adm. Code.

Information Technology

The examination revealed that the company does not require users to change their passwords periodically. The requirement to periodically change passwords reduces the company's exposure to unauthorized access. It is recommended that the company require all passwords be changed periodically, at least on a quarterly basis.

Compulsory Surplus Requirement

As noted in the section of this report captioned "Financial Requirements," HMOs are required to maintain minimum compulsory surplus. The HMO's calculation as of December 31, 2002, is as follows:

Assets	\$ 77,560,368	
Less:		
Special deposit	2,330,000	
Liabilities	<u>55,370,999</u>	
Total		\$19,859,369
Net premium earned	285,800,679	
Compulsory factor	<u>3%</u>	
Compulsory surplus		<u>8,574,020</u>
Compulsory Excess		<u>\$11,285,349</u>

IX. CONCLUSION

Security Health Plan of Wisconsin, Inc., is a nonprofit, network health maintenance organization insurer serving central and northern Wisconsin. The HMO is sponsored and controlled by the Marshfield Clinic through representation on the board, service contracts, and common management. The company offers comprehensive HMO coverages for groups, individuals, and Medicare-eligible persons.

Since the last examination, as of December 31, 1997, the reported assets increased from \$39.6M to \$77.6M and liabilities increased from \$29.6M to \$55.4M. These amounts represent increases of 96% and 87%, respectively. The company's enrollment increased 21% in 2000 however, has declined slightly in 2001 and 2002. Overall premium has increased 81% from \$141.0M to \$255.2M.

As a result of the examination, no adjustments or reclassifications were made. Seven recommendations were made on a variety of issues and are listed on the following page.

X. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 25 - Annual Statement—It is recommended that the company properly fill out the jurat page in accordance with the NAIC Annual Statement Instructions – Health pursuant to s. Ins 50.20, Wis. Adm. Code.
2. Page 25 - Annual Statement—It is recommended that the company complete the Underwriting and Investment Exhibit – Part 2D, in accordance with the NAIC Annual Statement Instructions – Health pursuant to s. Ins 50.20, Wis. Adm. Code.
3. Page 25 - Annual Statement—It is recommended that the company report the actual amount on deposit with the State Treasurer on Schedule E – Part 2, regardless of the amount required by statute as stated in the NAIC Annual Statement Instructions – Health.
4. Page 26 - Company Agreements—It is recommended that the company amend its agreements with Marshfield Clinic to include indemnification and/or hold harmless provisions.
5. Page 26 - Investments—It is recommended the company establish procedures to have investment transactions formally approved by the board of directors.
6. Page 26 - Record Retention—It is recommended that the company retain the appropriate records according to s. Ins 6.80, Wis. Adm. Code.
7. Page 27 - Information Technology—It is recommended that the company require all passwords be changed periodically, at least on a quarterly basis.

XI. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the HMO is acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance (OCI), State of Wisconsin, participated in the examination:

Name	Title
Bridgot Quandt	Insurance Financial Examiner
Randy Milquet	Insurance Financial Examiner - Advanced

Respectfully submitted,

Sonja M. Dedrick
Examiner-in-Charge